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IN THE

Supreme Court of the United States

October Term, 195

No. [redacted] 128

A. J. OSTHEIMER, 3RD, RUTH M. OSTHEIMER,
Petitioners

v.

THE UNITED STATES OF AMERICA,
Respondent

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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INDEX

	Page
Opinions below	2
Jurisdiction	2
Questions presented	2
Constitutional provision and statute involved	3
Statement	3
Reasons for granting the writ	5
Conclusion	9
Appendix A—Opinion of District Court Below	10
Appendix B—Opinion of Court of Appeals Below	12

CITATIONS

Benjamin v. Hoey, 132 F. 2d 945 (2d Cir. 1944)	7, 8
Burnet v. Harmel, 287 U.S. 103, 53 S.Ct. 74 (1932)	9n
Kenneth W. Daehler, 31 T.C. No. 73 (1959)	7
Sol Minzer, 31 T.C. No. 115 (1959)	7

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v.

THE UNITED STATES OF AMERICA,
Respondent

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Alfred J. Ostheimer, 3rd, and Ruth M. Ostheimer petition for a Writ of Certiorari to review the judgment of the United States Court of Appeals for the Third Circuit entered March 9, 1959, affirming the decision of the United States District Court for the Eastern District of Pennsylvania.

CITATIONS TO OPINIONS BELOW

The memorandum opinion of the District Court, printed in Appendix A hereto, p. 10, is reported in 160 F. Supp. 669.

The opinion of the Court of Appeals, printed in Appendix B hereto, p. 12, is reported in 264 F. 2d 789.

JURISDICTION

The judgment of the Court of Appeals was entered on March 9, 1959. A Petition for Rehearing was timely filed on March 24, 1959, and was denied on March 31, 1959. The jurisdiction of this Court is invoked under Section 1254(1) of the Judicial Code, 28 U. S. C. Section 1254(1) (1952).

QUESTIONS PRESENTED

1. Does a life insurance broker who pays premiums on policies of life insurance which he purchased for himself realize taxable income in an amount equal to the contractual commissions on such premiums which are returned to him by the insurance company?

2. Does a life insurance broker who pays premiums on policies of life insurance which he purchased for his children realize taxable income in an amount equal to the contractual commissions on such premiums which are returned to him by the insurance company?

CONSTITUTIONAL PROVISION AND STATUTE INVOLVED

The question presented involves the meaning of "income" in the Sixteenth Amendment to the Constitution of the United States, as applied through Section 22(a) of the Internal Revenue Code of 1939, 26 U. S. C. Section 22(a) (1952).

Sixteenth Amendment:

> "The Congress shall have power to lay and collect taxes on incomes, from whatever sources derived, without apportionment among the several States, and without regard to any census or enumeration."

Section 22(a):

> " 'Gross income' includes gains, profits, and income derived from salaries, wages, or compensation for personal service (including personal service as an officer or employee of a State, or any poltitical subdivision thereof, or any agency or instrumentality of any one or more of the foregoing), of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. . . ."

STATEMENT

Suit was filed in the United States District Court for the Eastern District of Pennsylvania for a refund of income taxes, and interest thereon, paid for the years 1947, 1948

and 1949.[1] The jurisdiction of the District Court was invoked under Section 1346(a)(1) of the Judicial Code, 28 U. S. C. Section 1346(a)(1) (1952).

During the years 1947, 1948 and 1949, A. J. Ostheimer, 3rd (hereinafter called the "taxpayer") was, and has continued to be, a life insurance broker, licensed in Pennsylvania and other states. The taxpayer conducted a sole proprietorship in Philadelphia, Pennsylvania, except during the first seven months of 1947 when he conducted business in a partnership.

The taxpayer purchased and was the owner of policies of insurance on the lives of his partner and three key employees. The taxpayer also purchased policies of insurance on the lives of four of his children. He gave these policies to the children, who were thereby made the owners. All but one of the policies were issued by the Northwestern Mutual Life Insurance Company (hereinafter called "Northwestern"). The remaining policy was issued by Aetna Life Insurance Company (hereinafter called "Aetna").

The taxpayer paid standard gross premiums on these policies. The insurance companies returned to the taxpayer amounts equal to the contractual commissions on the gross premiums.

The taxpayer did not include the amounts so returned to him by the insurance companies in his taxable income for the years in question. The Revenue Officials later added these amounts to the taxpayer's income and collected the resulting tax. The present suit for refund was thereafter duly commenced.

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[1] The exact sum of income taxes and interest paid on the amounts here in issue has not been determined. The amounts of alleged income here in issue are: 1947—$517.89; 1948—$328.85; 1949—$1,022.04. (R. Appendix, p. 42a.) It has been stipulated that if appellants are entitled to refund, the net refund will be determined as agreed upon by the parties, and that if the parties are unable to agree, the matter will be submitted for determination by the district court. (R. Appendix, p. 8a.)

The taxpayer here was an authorized representative in Pennsylvania for nine insurance companies other than Northwestern and Aetna. Neither Northwestern nor its General Agent in Philadelphia prescribed rules governing the development of the taxpayer's clientele. The taxpayer could go and come as he pleased. He was not required to spend a fixed amount of time for Northwestern. (R. Appendix p. 53a). He was obligated to give Northwestern a right of first refusal on policies of the type written by Northwestern. (R. Appendix pp. 61a-63a). Applying the common-law rules than prescribed by the Social Security Act for determining employer-employee relationship, the Chief Counsel of the Bureau of Internal Revenue held, in 1937, that a Special Agent of Northwestern, like the taxpayer, was not an employee but an independent contractor. (R. Appendix p. 33a).

REASONS FOR GRANTING THE WRIT

1. *The case presents a constitutional question of far-reaching importance in the administration of the Federal income tax.*

We believe that the basic issue is whether the comparative economic advantage which a person is able to obtain as an incident inherent in his particular calling constitutes taxable income. In the case at bar, the taxpayer happens to be an insurance broker. As an incident to that calling, the out-of-pocket costs for insurance he himself buys and pays for will be less than the costs of corresponding policies to a person who is not in the insurance business.

Illustrations of everyday transactions where a comparative economic advantage is obtainable simply as an incident of a person's own occupation are virtually limitless. An example is found in the legal profession. A frequent and well-known practice among law firms is to give a law associate a fixed percentage of any fee paid to the law firm by a

personal client of the associate. As an example, let us assume that a young attorney associated with a law firm is himself injured in an automobile accident. He turns his claim over to the firm's litigation specialists who obtain a $12,000 judgment. The firm's fee for its services in a negligence case of this type is 30% of the judgment, or $3,600. As in the case of one of his personal clients, the associate is entitled to receive one-third of the gross fee, $1,200, for "bringing in" the case—his own case—to the office. The firm, following its normal accounting procedures, collects its $3,600 fee from the associate and gives him one-third of what he paid in, or $1,200, at the end of the next accounting period.

If the Court of Appeals' decision in the instant case is correct, it seems clear that our young attorney would have $1,200 of taxable income despite the fact that the generating source of the whole fee of $3,600 was money paid into the firm by the young attorney himself.

The law associate who brings his own case to his law firm, the real estate broker who buys a home for himself and family, the stockbroker who buys or sells securities as part of his own investment program, the insurance broker who pays premiums for his own purposes—each is able to consummate his own transaction at lower out-of-pocket costs than would a member of the general public. It is the taxpayer's position that the comparative economic advantage to each is simply the normal, commonplace advantage that a person in a particular occupation has over a person in a different occupation. Whether we call it "an inherent incident of one's occupation," or "getting it wholesale," the net effect is the same—a lower out-of-pocket cost. We submit that this net effect is a true reduction in cost—*not* taxable income.[2] One does not produce taxable income by "selling something to himself."

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[2] The issue here is not to be confused with the question of the taxability of an employee's bargain purchase or an employee's discount. Beyond the fact that the insurance broker in the instant case

In recent months, the basic issue involved here has been litigated in two other cases. Because of the widespread impact of the issue, it is not unreasonable to expect further litigation.

These recent decisions create a sharp division of opinion. In *Sol Minzer*, 31 T. C. No. 115, the Tax Court, by a 10-6 vote, reached a conclusion directly contrary to that of the Court of Appeals in the instant case. The *Minzer* decision was handed down only four days after the opinion of the Court of Appeals here. Similarly, in *Kenneth W. Daehler*, 31 T. C. No. 73 (Jan. 12, 1959), the Tax Court held, by a 10-5 vote, that a real estate broker was not taxable on the amount equal to the "commission" on the sale of property he purchased for his own use.

For the foregoing reasons, we respectfully urge that it would be in the public interest for this Court to settle the issue at this time and, in so doing, forestall what would seem to be an almost inevitable flood of litigation in a matter of nationwide importance.

2. *The decision of the court below conflicts in principle with the decision of the Court of Appeals for the Second Circuit in Benjamin v. Hoey, 139 F. 2d 945 (1944).*

In *Benjamin*, the taxpayer, a 38% partner in a stock brokerage firm, purchased and sold securities through the firm for his personal account and paid to the partnership the full, usual commissions on each transaction. The Court of Appeals held that the taxpayer's percentage of the commissions was not taxable income to him.

> "Because he had partners, he paid out an amount equal to 62% of the commissions. The balance, 38%,

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is not an employee, an employer, in the standard case of an employee discount, retains less than he would from a sale of a similar item to the general public. In the instant case, the insurance company retained every last dollar from the premium paid by the insurance agent that it ever expected to retain in insuring any other person who presented the same actuarial risk.

or $25,439.91, always remained his. To put it differently, that sum he paid to himself, and what one pays to oneself cannot be part of one's income." 139 F. 2d 2d at 946.

The court below expressed the view that the *Benjamin* case could be distinguished on the ground that the taxpayer there was a member of a partnership and had thus, in a sense, paid the money "to himself." But the underlying factors in *Benjamin* are equally applicable to the instant case. In both cases, the taxpayer knew before the transaction commenced that he was entitled to the return of a specific percentage of amounts which he originally paid out in full from his own pocket for his own purposes. Each was able to obtain this economic advantage simply because of his particular occupation.

We cannot perceive any purpose or policy which, at the constitutional level, permits one tax result for the stockbroker and a different one for the insurance broker. We submit that such distinctions as there are between the two brokers lack relevance to the constitutional issue and that there is thus a basic conflict between the Second Circuit and the Third Circuit in the application of the Constitution. We can indeed be sure that neither the stockbroker nor the insurance broker will ever comprehend why the one should be treated differently from the other.

3. *The implication of the decision below conflicts with the applicable decisions of this Court, in that the court below relied upon state law in determining the concept of "income" under the Constitution.*

The court below made pointed reference to a Pennsylvania statute which prohibits "rebates" on insurance premiums. It reasoned that since the lower cost incurred by the taxpayer could not legally be the result of a "rebate"

under state law, the economic benefit must be taxable income under the United States Constitution.[3]

It is axiomatic that state law cannot control the operation of a Federal income tax statute unless the Federal statute itself clearly permits such control. It is the "will of Congress . . . to give a uniform application to a nationwide scheme of taxation."[4] *A fortiori*, a constitutional issue as to the meaning of "income" cannot be made to depend upon the langauge used by a state legislature.

Moreover, whether a state statute permits a "rebate" to an insurance broker on his personal premium payments or simply permits the "usual commission" thereon, the broker has the identical comparative economic advantage over a member of the general public. In either case, the application of the United States Constitution to the issue presented here must remain the same. We, accordingly, submit that reference to the terminology of state insurance laws really begs the issue of Federal taxation under the Sixteenth Amendment.

Conclusion

For the foregoing reasons, this Petition for a Writ of Certiorari should be granted.

Respectfully submitted.

MERVIN M. WILF,
BERNARD V. LENTZ,
HERBERT W. REISNER,
Counsel for Petitioners

Dated: June 15, 1959

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[3] 264 F. 2d at 792, Appendix B, at pp. 16-17.

[4] Burnet v. Harmel, 287 U. S. 103, 110, 53 S. Ct. 74, 77 (1932).

Appendix "A"

OPINION OF THE DISTRICT COURT

Kirkpatrick, *Chief Judge:*

The plaintiff, a life insurance agent authorized to act as special agent for the Northwestern Mutual Life Insurance Company and to solicit for the Aetna Life Insurance Company, procured policies with Northwestern on the lives of his former partner, three key employees and his children, as well as one with Aetna on the life of his former partner. He brings this suit to recover the additional tax paid because of the inclusion in his income, by the revenue officials, of the commissions he received from the insurance companies by reason of the issuance of these policies. He contends that these commissions were not income to him but were, in effect, a reduction of the price of the policies.

I cannot agree. The Internal Revenue Department ruled in 1915 (T. D. 2137, 17 Treasury Decisions 48) that "A commission retained by a life insurance agent on his own life insurance policy is held to be income accruing to the agent, and should be included in his return of income for the assessment of the income tax." This ruling was reaffirmed in 1932 and again in 1955. Obviously, the ruling would be the same as to commissions on policies on the lives of an agent's children, his employees and his business partner.

An administrative interpretation such as this, so consistently followed over such a long period of time, is entitled to great weight with the Court and there is a heavy burden upon the plaintiff to show that it is erroneous. The insurance company, in fact, pays its agent for procuring policies and the premiums thereon. This is what the plaintiff did. It is true that because the policies were upon the lives of his partner, his employees and members of his

family, he did not have to perform some of the duties that he would have performed if they had been upon the lives of strangers, but this in no way affects the status of the money he received. In fact, it would be a violation of the law for an insurance company to have sold insurance to him at a lower rate than that charged other policyholders.

Judgment may be entered for the defendant.

The requests for findings of fact and conclusions of law submitted by the defendant are all affirmed.

Appendix "B"

OPINION OF THE COURT OF APPEALS FOR THE THIRD CIRCUIT

By KALODNER, Circuit Judge:

Are commissions received by a life insurance agent on premiums which he paid on policies he had placed on the lives of his partner, key employees and children, "gross income" under Section 22(a) of the Internal Revenue Code of 1939? [1]

That is the single question presented by this appeal from the judgment of the District Court [2] which answered it affirmatively, in rejection of the contention that the commissions were merely a reduction of the cost of the policies.

The facts, critical to this appeal, may be summarized as follows:

During 1947, 1948, and 1949, the tax years here involved, A. J. Ostheimer, 3rd ("taxpayer") [3] conducted a business as a life insurance agent. During the first seven months of 1947, the business was conducted in partnership with one Earl Zebley, and thereafter as a sole proprietorship.

Taxpayer, during the years stated, was licensed to act as a life insurance agent in Pennsylvania for eleven life insurance companies. Among them were the Northwestern Mutual Life Insurance Company of Milwaukee, Wisconsin ("Northwestern"), of which he was a "Special Agent", and the Aetna Life Insurance Company ("Aetna").

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[1] 26 U. S. C. 1952 ed., Sec. 22.

[2] The opinion of the District Court is reported at E. D. Pa. 1958, 160 F. Supp. 669.

[3] Since a joint tax return was filed by taxpayer and his wife, Ruth M. Ostheimer, she is a party plaintiff.

Under his contracts with these insurance companies, the taxpayer was to receive commission on all life insurance business he wrote for them. By the contracts, as well as by Pennsylvania statutes,[4] the companies and their agents were required to sell insurance at fixed prices without rebate of premiums or commissions.

During the taxable years involved, taxpayer was the owner and beneficiary of life insurance policies which he had purchased on the lives of his business partner, Zebley, and three of his key employees. Four of his children also owned policies issued on their lives which were purchased by taxpayer and given to them. All but one of the policies were issued by Northwestern, the remaining one was issued by Aetna.

Taxpayer personally, and through his secretary, prepared the applications for the policies on which he was designated as agent. From the dates of their issuance, including the taxable years involved, he paid the standard premiums on all the policies, by checks drawn on his personal bank account. The policies and premium payments were processed by the general agents of Northwestern and Aetna in the same manner as other policies and premiums. The general agents periodically submitted "Commission Statements" to taxpayer and these statements covered all amounts due him from time to time, and were accompanied by checks for the total amount then due, including among others the regular commissions on the policies here involved.

Taxpayer was a "Special Agent" of Northwestern and an "authorized agent" for Aetna. As "Special Agent" taxpayer was not required to spend a fixed amount of time

[4] The Act of May 17, 1921, P. L. 789, Art. VI, §§635-636, 40 P. S. §§275-276 (Purdon 1954) provides that an insurance agent may not rebate any part of an insurance premium or his commission thereon; the Act of May 17, 1921, P. L. 682, Art. III, Sec. 346, 40 P. S. Sec. 471 (Purdon 1954) provides that insurance companies are prohibited from offering or making rebates on insurance premiums.

for Northwestern. He was obligated to give Northwestern a right of first refusal on policies of the type issued by it. His ageney contract specifically provided that it did not create an employer-employee relationship.

Taxpayer (and his wife) did not include in their gross income on their tax returns any of the amounts equal to contractual commissions on the policies involved. It may be noted, parenthetically, that taxpayer deducted as necessary and ordinary business expenses the nominal expenses incident to the policies agreed to be in the amount of $5.00 per annum.

The Commissioner determined that the commissions received by taxpayer on these policies should properly have been included in the taxable years at issue and accordingly assessed deficiencies. The District Court, as stated, sustained the Commissioner's determination.

Here, as below, taxpayer urges that his commissions merely effectuated a reduction of his cost in purchasing and maintaining the policies and consequently did not constitute "income". He says he merely acted as his own middleman and thereby obtained the middleman's benefit, viz., the commissions, enabling him to obtain the insurance "at a net price" or "wholesale".

Otherwise stated, taxpayer's contention is that the commissions he received on the premiums he paid were simply his "discount", and "discount" he says, is not income.

In reply, the government contends (1) the facts do not establish a bargain purchase of insurance since taxpayer paid the gross price required by law to be charged all insurance purchasers; and (2) even if a bargain purchase could be established by viewing the commissions as a reduction of purchase price, taxpayer secured a benefit by virtue of his employment relationship, not otherwise available to the public, which is clearly taxable as income.

We are in agreement with the government's view that the facts do not establish a bargain purchase so that consideration of its second contention is unnecessary.

We are further of the opinion that the commissions received by taxpayer on the policies here involved are well within the definition of "gross income" as stated in Section 22(a) of the Internal Revenue Code of 1939, and the specific language of Section 29.22(a)-2 Treasury Regulations 111 and Treasury rulings later discussed.

"Gross income", under the "General Definition" in Section 22(a), "includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * * of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales * * * and income derived from any source whatever".

The Treasury Regulations cited, under the caption "Compensation for Personal Services" provide:

> "Commissions paid salesmen, compensation for services on the basis of a percentage of profits, *commissions on insurance* * * * are income to the recipients * * *" (emphasis supplied).

Applicable to the instant appeal are these well-settled principles:

> "* * * in defining 'gross income' as broadly as it did in §22(a) Congress intended to 'tax all gains except those specifically exempted' ".[5]

> "The broad sweep of this language [Section 22(a)] indicates the purpose of Congress to use the *full measure of its taxing power* within those definable categories * * * Hence our construction of the statute should be consonant with that purpose. Technical considerations * * * or the legal paraphernalia which in-

[5] Commissioner of Internal Revenue v. Lo Bue, 1956, 351 U. S. 243, 246, 76 S. Ct. 800, 803, 100 L. Ed. 1142, rehearing denied 352 U. S. 859, 77 S. Ct. 21, 1 L. Ed. 2d 69, citing Commissioner of Internal Revenue v. Glenshaw Glass Co., 348 U. S. 426, 429-430, 75 S. Ct. 473, 99 L. Ed. 483, rehearing denied 349 U. S. 925, 75 S. Ct. 657, 99 L. Ed. 1256.

ventive genius may construct * * * should not obscure the basic issue." [6] (emphasis supplied)

"Where the payment is in return for services rendered * * *," such payment is gross income under Section 22(a).[7]

In the instant case the life insurance companies paid taxpayer commissions on the premiums as compensation for his services in placing the policies involved. The payments were in discharge of the contractual obligation of the insurance companies to pay taxpayer commissions on all premiums paid on policies which he wrote. In other words, the commissions were a "payment in return for services rendered", and as such constituted "gross income".

The payments were not "rebates" to taxpayer by the insurance companies, because, as earlier pointed out, Pennsylvania statutes prohibit the companies from making rebates on insurance premiums. The insurance companies were required by Pennsylvania statute to sell insurance to the public at fixed or uniform rates and taxpayer as a licensed insurance agent was likewise required by statute and by contract to sell at the fixed rates and not to rebate his commission.

Taxpayer, as required by Pennsylvania law and the provisions of the policies, paid the gross premiums on the policies to the insurance companies, and in usual course in accordance with his agency contracts, received the standard commissions on the premiums. Had taxpayer not been the agent who placed the policies he would not, and could not, have received the commissions on the premiums. It was

[6] Hevering v. Clifford, 1940, 309 U. S. 331, 334, 60 S. Ct. 554, 556, 84 L. Ed. 788. See also Commissioner of Internal Revenue v. Glenshaw Glass Co., note 5 supra.

[7] Robertson v. United States, 1952, 343 U. S. 711, 714, 72 S. Ct. 994, 996, 96 L. Ed. 1237; Teleservice Co. of Wyoming Valley v. Commissioner, 3 Cir., 1958, 254 F. 2d 105, 112, certiorari denied 1958, 357 U. S. 919, 78 S. Ct. 1360, 2 L. Ed. 1364.

only in his capacity as agent that he was paid these commissions.

The mere circumstance that taxpayer paid the premiums out of his own funds had no bearing on the nature of the commissions received by him on these premiums.

The circumstance that the commissions operated to reduce the out-of-pocket premium outlays could not operate to make the policy purchases and maintenance "discount" transactions.

In its dealings with taxpayer the insurance companies dealt with him solely as an agent and not as a "customer" or "middleman". Neither as "customer" or "middleman" could they have given him a "discount" because such a "discount" would have been a proscribed "rebate".

The cases cited by taxpayer are inapposite. Take for example, Benjamin v. Hoey, 2 Cir., 1944, 139 F. 2d 945. There the taxpayer was a 38% partner in a stock brokerage firm. He purchased and sold securities through the firm for his personal account and paid to it the usual brokerage commissions on his transactions. Both the District Court [8] and the Court of Appeals held that the taxpayer's share of his own commissions was not taxable income. The holding was premised on the fact that "what one pays to one's self cannot be part of one's income." 139 F. 2d at page 946. With respect to the holding in the Benjamin case it need only be said that it is distinguishable on its facts. There the taxpayer paid his share of the commissions to himself while in the instant case he paid the premiums not to himself but to the insurance companies. Here, taxpayer and the insurance companies were separate entities. There was no partnership relationship between them, only a contractual principal-agent relationship.

Taxpayer has called our attention to Kenneth W. Daehler, 31 T. C. —. There it was held (five judges dissenting) that the amount refunded to a real estate salesman

[8] Reported at S.D.N.Y. 1942, 47 F. Supp. 158.

by his employer as salesman's share of commission on a house the salesman himself bought constitutes a reduction of the price paid for the house rather than taxable income. With respect to this case we need but say that we do not subscribe to its holding. As the dissenting judges pointed out, the salesman's commission was "an employee's commission paid to him for personal services rendered by him to such [his] employer" and, "This compensation for services rendered, definitely constituted gross income under Section 22(a) of the 1939 Code."

There remains only this to be said.

The District Court in its opinion, 160 F. Supp. 669 stated:

> "The Internal Revenue Department ruled in 1915 (T. D. 2137, 17 Treasury Decisions 48) that 'A commission retained by a life insurance agent on his own life insurance policy is held to be income accruing to the agent, and should be included in his return of income for the assessment of the income tax.' This ruling was reaffirmed in 1932[9] and again in 1955.[10] Obviously, the ruling would be the same as to commissions on policies on the lives of an agent's children, his employees and his business partner.
>
> "An administrative interpretation such as this, so consistently followed over such a long period of time, is entitled to great weight with the Court and there is a heavy burden upon the plaintiff to show that it is erroneous."

We subscribe to the District Court's statement.

Administrative interpretations are of great persua-

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[9] G. C. M. 10486, XI-1 Cum. Bull. 14 (1932).

[10] Rev. Rul. 55-273, 1955-1 Cum. Bull. 221.

sion in deciding an issue of statutory construction. See Saunders v. Commissioner, 3 Cir., 1954, 215 F. 2d 768.

Taxpayer contends that he was an independent contractor.

As to this contention it need only be said that the contracts between taxpayer and the insurance companies are forms of employment. The record discloses in fact that Northwestern paid social security taxes with respect to taxpayer's services.

Independent of what has been said, taxpayer certainly had no possible basis for his contention that he was acting as "middleman" with respect to the premiums paid on the policies owned by his children. The premium payments which he made on his children's policies were "gifts" to the children, nothing more, nothing less. The fact that his commissions operated to reduce the cost of his gifts did not change the character of the commissions as compensation to him for his services as agent.

For the reasons stated the judgment of the District Court will be affirmed.

JUDGMENT

This cause came on to be heard on the record from the United States District Court for the Eastern District of Pennsylvania and was argued by counsel

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the said District Court in this case be, and the same is hereby affirmed.

Attest:

IDA O. CRESKOFF
Clerk

March 9, 1959

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ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF *AMICUS CURIAE*, ON BEHALF OF THE NATIONAL ASSOCIATION OF LIFE UNDERWRITERS

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June , 1959.

INDEX

	PAGE
Opinions below	2
Jurisdiction	2
The question presented	2
Statute and regulations involved	2
Summary statement of the case	3
Reasons for the allowance of the writ	3
Conclusion	9
Appendix	11

Citations

Benjamin v. *Hoey*, 139 F. 2d 945 (2d Cir. 1944)	5, 6, 7
Eisner v. *Macomber*, 252 U. S. 189	4, 5, 7
James William Everhart, 26 B.T.A. 318 (1932)	7
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BRIEF *AMICUS CURIAE*, ON BEHALF OF THE NATIONAL ASSOCIATION OF LIFE UNDERWRITERS

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

The National Association of Life Underwriters hereby joins with A. J. Ostheimer and Ruth M. Ostheimer, the Petitioners herein, in petitioning for a writ of certiorari to review a decision of the Court of Appeals for the Third Circuit, affirming a decision of the District Court for the Eastern District of Pennsylvania, denying refunds of the Petitioners' Federal income taxes for the years 1947, 1948 and 1949.

Consent to the filing of this brief as *amicus curiae* was granted by the Solicitor General on behalf of the Respondent in its letter dated June 9, 1959 (Appendix A). Consent was granted by the Petitioners in the letter from their counsel dated June 23, 1959 (Appendix B).

Opinions Below

The opinion of the District Court (Eastern District of Pennsylvania) is reported at 160 F. Supp. 669 (Appendix A to Petition). The decision of the United States Court of Appeals for the Third Circuit is reported at 264 F. 2d 789 (Appendix B to Petition).

Jurisdiction

The jurisdiction of this Court is invoked under Section 1254(1) of the Judicial Code, 62 Stat. 928 (1948), 28 U.S.C. §1254(1).

The Question Presented

The sole question for determination is whether taxable income is realized by a life insurance agent or broker upon the purchase of policies of life insurance for his own benefit, as a result of the fact that the premiums for such policies are reduced by an amount equivalent to the commission which the agent or broker receives or would have received had policies been sold to third parties.

Statute and Regulations Involved

The only statutory provision involved in this proceeding is Section 22(a) of the Internal Revenue Code of 1939 (Int. Rev. Code of 1939, ch. 2, §22(a), 53 Stat. 9, as amended). The aforesaid statute is set forth in the Petition at page 3. No Treasury Regulation is involved.

Summary Statement of the Case

Throughout the years 1947, 1948 and 1949 the Petitioner, A. J. Ostheimer, 3rd, was a licensed life insurance "agent" and "broker" authorized to act for eleven life insurance companies. During the taxable years involved the aforesaid Petitioner purchased, and was the beneficiary of, life insurance policies on the lives of his business partner, three of his key employees, and four of his children. The Petitioner personally paid the standard premiums on all of such policies. By reason of his position as "agent" and "broker" the issuing companies subsequently paid to him amounts equivalent to the "commissions" attributable to the sale of such policies. The Petitioner did not include any of such "commissions" in his Federal income tax returns (filed jointly with his wife) for the taxable years in question. The Commissioner of Internal Revenue determined that such "commissions" constituted income and assessed deficiencies which were paid by the Petitioner. Appropriate claims for refund subsequently were filed by the Petitioner and, upon the denial thereof by the Commissioner, action was instituted by the Petitioner in the District Court.

Reasons for the Allowance of the Writ

1. The Question Presented Affects Many Taxpayers.

The National Association of Life Underwriters (the "Association"), which asks leave to appear in this proceeding as *amicus curiae*, is a non-profit trade association whose membership consists of approximately 80,000 full-time life insurance agents. The Association's records indicate that there are approximately 200,000 full-time life insurance agents in the United States. Although no exact

statistics are available, it is understood that the vast majority, if not all, of the full-time life insurance agents within the United States from time to time purchase life insurance for their own benefit upon their lives, their families' lives and the lives of their business associates. Accordingly, the question which the Court is requested to review here is one of universal interest and application to a large segment of the American taxpayers. Moreover, it may not be said that the problem is *de minimis* inasmuch as the reduction in premiums which a life insurance agent or broker obtains upon the purchase of policies for his own benefit is substantial and if such reduction were to be viewed as taxable income, as the Respondent here maintains, the tax attributable thereto would be substantial.

2. The Issue Requires a Judicial Delineation of the Scope of the Generic Concept of Taxable Income.

The decision of the Court below represents an unprecedented extension of the concept of taxable income as defined by this Court in *Eisner* v. *Macomber*, 252 U. S. 189. In essence, the Court below has determined that an individual may realize taxable income from services rendered to himself. Historically, the concept of taxable income has been limited to the gain derived from capital or labor or both combined. Prior to the decision of the Court below it has not been suggested that this concept could be extended to cover the indirect benefits inherent in one's occupation or profession. Nor has there been any suggestion that taxable income is generated by labor done or services rendered by an individual for his own benefit. May it be said that a real estate broker realizes income where by reason of his calling he is enabled to buy or sell his own home without incurring the usual broker's commissions? Similarly, does an attorney or doctor who

advises or prescribes for himself or his family incur tax liability?

Other examples of so-called inherent occupational benefits are numerous: the automobile dealer or salesman who may purchase a vehicle at a price substantially below the prevailing price to the public; the department store employee who receives the traditional employee discount upon purchases; and the farmer to whom produce is available at a price substantially below its current market price. Surely such benefits are not within the established historical concept of taxable income. Indeed, if the rationale adopted by the Court below were extended to its logical limits, practically all self-benefiting endeavor would generate taxable income irrespective of its compensatory aspects. Such a result would have the effect of a creeping paralysis upon the economy of this country and upon the initiative of its population and must be avoided.

It is therefore respectfully submitted that it is the province of this Court again to define, as was done in *Eisner* v. *Macomber, supra,* the limits beyond which the hands of the Tax Collector cannot reach.

3. The Decision of the Court Below Is in Conflict with the Decision of the Court of Appeals for the Second Circuit in *Benjamin* v. *Hoey,* 139 F. 2d 945 (1944).

In *Benjamin* v. *Hoey* the Court of Appeals for the Second Circuit was required to determine the question of the taxability of a stock broker on commissions paid to his own brokerage firm in respect of stock purchases by him for his own account. The Court there held that the broker's distributable share of such commissions did

not constitute taxable income to him. In so holding, the Second Circuit stated (p. 946):

> "If without partners, he had conducted the brokerage business, he would have paid the entire amount of those commissions to himself and no one would then have thought of saying that those payments constituted part of his taxable income. * * * [W]hat one pays to one's self cannot be part of one's income."

The only distinction between the *Benjamin* case, *supra*, and the instant situation is the immaterial difference that the former involved a stock broker while the latter involves a life insurance broker. The *Benjamin* case is therefore direct authority for the position which the Petitioners have maintained throughout these proceedings. It is submitted that the decision of the Court below is in direct conflict with the decision of the Second Circuit in the *Benjamin* case and such conflict should be resolved by this Court.

4. The Decision of the Court Below Is Erroneous as a Matter of Law.

"Commissions"[1] realized by a life insurance agent on life insurance policies which he buys for his own benefit are a reduction in the cost of the policies, realized on account of his particular occupation. These reductions-in-cost are a payment to himself and represent also an "occupational benefit" enjoyed by him because of his vocation.

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1. Because labels or semantics seem to play such a large part in the decision of this case, it is suggested that an accurate term for this benefit would be a "reduction-in-cost". To place upon these reductions-in-cost one of the labels frequently given them by the Commissioner, such as a commission, fringe benefit, bargain purchase, etc., begs the question of whether they are income to the taxpayer.

The reduction-in-cost is a payment by the agent to himself.

No court has ever held that payments to one's self constituted income. *Eisner* v. *Macomber*, 252 U. S. 189, originally defined income as any "gain derived from * * * labor." Subsequent decisions have made clear that gains or benefits produced for one's own use (as when a lawyer draws his own will) are not taxable income. *Benjamin* v. *Hoey, supra*, decided this exact question in holding that to tax a stock broker's commissions paid to his own brokerage firm in respect of stock purchases for his own account would be to tax payments made to himself.

The same result was reached in *James William Everhart*, 26 B.T.A. 318 (1932), which held nontaxable the reduction in cost realized by a salesman of participation interests in oil syndicates, when he "purchased" them for himself less his commission; in *Kenneth W. Daehler*, 31 T.C. No. 73 (1959), holding a real estate agent's "commissions" on his own purchases not taxable; and in *Sol Minzer*, 31 T.C. No. 115 (1959), discussed below, holding nontaxable an insurance agent's commissions on his own insurance.

Reduction-in-cost is a benefit occasioned by an insurance salesman's occupation.

Mr. Ostheimer was able to get this reduction-in-cost solely because of his occupation. It is inherent in his calling—the same as are free medical services to a physician, or commission-free real estate to a realtor.

In holding that insurance "commissions" on policies acquired by an insurance agent for his own benefit do not constitute taxable income, the United States Tax Court in

Sol Minzer, 31 T.C. 115 (1959) (reviewed by the whole court) stated this conclusion:

> "Of pivotal significance here is the fact that petitioner derived an economic benefit merely as an incident to his status as an insurance broker, similar to the economic benefits that might accrue to the persons described in the foregoing examples [stock broker, realtor], and the reason that such benefits are not regarded as taxable income is that they are not compensatory in nature."

It is recognized that the taxation of employer provided fringe benefits which are, and are intended to be, compensation may be justified in certain instances. Such situations are to be distinguished, however, from those non-compensatory benefits which inure to an individual solely as a result of his particular occupation, profession or calling. Any radical changes in the taxation of such latter benefits should be applied equally to all taxpayers rather than solely to insurance agents.

If the decision of the Circuit Court should stand, a serious tax discrimination would exist against life insurance agents and brokers, as contrasted with people following all other occupations (e.g. stock brokers, realtors) in substantially the same position. As was asked so directly by Judge Mulroney in his concurring opinion in *Sol Minzer*, 31 T.C. No. 115 (1959):

> "If the salesmen of property, or of insurance other than life, realize no taxable income when they buy on their own behalf, why should there be a different rule for life insurance salesmen?"

Conclusion

For the foregoing reasons it is respectfully submitted that the petition for a writ of certiorari should be granted.

Respectfully submitted,

H. Gilmer Wells,
Orrie P. Stevens,
Counsel for The National Association of Life Underwriters as Amicus Curiae.

Of Counsel:
Carlyle M. Dunaway, *General Counsel,*
The National Association of Life Underwriters.

APPENDIX A

OFFICE OF THE SOLICITOR GENERAL
Washington, D. C.

H. Gilmer Wells, Esq.,
Cadwalader, Wickersham & Taft,
14 Wall Street,
New York 5, New York.

Re: *Ostheimer v. United States*

Dear Mr. Wells:

I have your letter of June 1, 1959, in which you request consent to file an *amicus* brief, on behalf of the National Association of Life Underwriters, in support of the petition for certiorari in the above-entitled case. In view of the representations contained in your letter, I am pleased to consent to your request. I am enclosing for your information a copy of a memorandum setting forth the Government's practice in matters of this kind.

Sincerely yours,

/s/ J. LEE RANKIN /by P. E.
J. Lee Rankin
Solicitor General

Enclosure

APPENDIX B

Law Offices
WHITE & WILLIAMS
19th Floor, Land Title Building,
Philadelphia 10, Pennsylvania.

June 23, 1959.

H. Gilmer Wells, Esq.,
Messrs. Cadwalader, Wickersham & Taft,
14 Wall Street,
New York 5, New York.

Dear Mr. Wells:

As counsel for Petitioners in the case of *Ostheimer* v. *United States*, No. 1014, October term 1958, we consent to your filing a brief *amicus curiae* on behalf of the National Association of Life Underwriters in favor the granting of the Petition for a Writ of Certiorari.

WHITE & WILLIAMS

s/ BERNARD V. LENTZ

By .....
Bernard V. Lentz

INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	2
Statutes and other authorities involved	2
Statement	2
Argument	6
Conclusion	13
Appendix	14

CITATIONS

Cases:

Benjamin v. *Hoey*, 139 F. 2d 945	10, 11, 12
Commissioner v. *Glenshaw Glass Co.*, 348 U. S. 426	7
Commissioner v. *LoBue*, 351 U. S. 243	12, 13
Commissioner v. *Smith*, 324 U. S. 177	12, 13
Commissioner v. *Webster Corp.*, 240 F. 2d 164	12
Dachler v. *Commissioner*, 31 T. C. No. 73	9
Lykes v. *United States*, 343 U. S. 118	9
Mass. Mutual Life Ins. Co. v. *United States*, 288 U. S. 269	9
Minzer v. *Commissioner*, 31 T. C. No. 115	9, 10
Robertson v. *United States*, 343 U. S. 711	8
Stern v. *Commissioner*, 215 F. 2d 701	10

Statutes:

Internal Revenue Code of 1939, Sec. 22(a) (26 U. S. C. 1952 ed., Sec. 22(a))	2, 7, 14
Internal Revenue Code of 1954, Sec. 7443 (26 U. S. C. 1952 ed., Supp. V, Sec. 7443)	10
40 Purdon's Pennsylvania Statutes, Annotated:	
Sec. 275	3
Sec. 471	3

Miscellaneous:

	Page
G.C.M. 10486, XI-1 Cum. Bull. 14 (1932)	2, 8, 15
Rev. Ruling 55-273, 1955-1 Cum. Bull. 221	2, 8, 17
T. D. 2137, 17 Treasury Decisions 48 (1951)	2, 8, 15
Treasury Regulations 111:	
Sec. 29.22(a)-1	2, 12, 13, 14
Sec. 29.22(a)-2	2, 7, 15
Sec. 29.22(a)-3	2, 12, 15

In the Supreme Court of the United States

OCTOBER TERM, 1959

No. 128

A. J. OSTHEIMER, 3RD, RUTH M. OSTHEIMER,
PETITIONERS

v.

THE UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the District Court (Pet. 10-11) is reported at 160 F. Supp. 669. The opinion of the Court of Appeals (Pet. 12-19) is reported at 264 F. 2d 789.

JURISDICTION

The judgment of the Court of Appeals was entered on March 9, 1959. (Pet. 19.) A timely petition for rehearing was denied on March 31, 1959. The peti-

tion for a writ of certiorari was filed June 19, 1959. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1254(1).

QUESTION PRESENTED

Whether commissions received by a life insurance agent, in the ordinary course of business, on premiums paid by him for life insurance policies which he purchased on the lives of his partners, his key employees and his children, constitute taxable income within the meaning of Section 22(a) of the Internal Revenue Code of 1939.

STATUTES AND OTHER AUTHORITIES INVOLVED

Section 22(a) of the Internal Revenue Code of 1939, Sections 29.22(a)-1, 29.22(a)-2 and 29.22(a)-3 of Treasury Regulations 111, Treasury Decision 2137, G.C.M. 10486 and Rev. Rul. 55-273 are set forth in the Appendix, *infra*, pp. 14-19.

STATEMENT

This action involves claims for refund of income taxes for the years 1947, 1948 and 1949. The facts, as found by the District Court (R. 72a-75a)[1], may be briefly summarized as follows:

During 1947, 1948 and 1949, A. J. Ostheimer, 3rd, hereinafter referred to as the taxpayer, conducted a

[1] This reference is to the findings of fact and conclusions of law proposed by the Government, defendant in the District Court. These proposed findings and conclusions were adopted by the District Court. (R. 77a.)

business as a life insurance agent. During the first seven months of 1947, the business was conducted in partnership with one Earl Zebley, and thereafter as a sole proprietorship. Among the insurance companies for which the taxpayer was licensed to act as agent in Pennsylvania were the Northwestern Mutual Life Insurance Company of Milwaukee, Wisconsin, and the Aetna Life Insurance Company. (R. 72a.)

Under his contracts with these insurance companies, the taxpayer was to receive commissions for all life insurance business he procured for the companies and which they accepted. Under the contracts, as well as by Pennsylvania statutes (40 Purdon's Pennsylvania Statutes, Annotated, Secs. 275 and 471), the companies and their agents were required to sell insurance at fixed prices without rebate of premiums or commissions. (R. 72a.)

During the taxable years, the taxpayer was the owner and beneficiary of four life insurance policies issued by Northwestern on the lives of his business partner and certain key employees. He also had procured from the same company life insurance policies for four of his children, which policies were given to such children. In addition, the taxpayer was the owner of one life insurance policy issued by Aetna on the life of his business partner. In connection with all of these policies, the taxpayer, personally and through his secretary, prepared the applications, arranged for the initial medical examinations, and remitted the premium checks to the companies. The taxpayer was designated as agent on all of the

aforementioned policies and he was entitled to receive from the insurance companies standard contractural commissions on all premiums paid. (R. 72a-73a.)

The taxpayer paid the standard premiums on all of the aforementioned policies by check drawn on his personal bank account. The policies were handled and treated by the general agents of Northwestern and Aetna in the same manner as other policies solicited by the taxpayer, and the commissions on such policies were remitted to the taxpayer in the same way as other commissions. The general agents of Northwestern and Aetna periodically submitted "Commission Statements" to the taxpayer at his place of business. These commission statements covered all amounts due him from time to time and were accompanied by checks for the total amounts then due, including, among others, the regular commissions on the policies referred to above. (R. 73a.)

Under the standard forms of agents' contracts used by Northwestern, the agent is ordinarily furnished free office space and stenographic services, or, in lieu thereof, is granted an extra commission. He is expected to work full time for the company. The company may at any time terminate the contract on thirty days' notice. The agent is considered by the company to be in a position of trust and responsibility on behalf of the company. And the agent, if he qualifies, is required to participate in the company retirement plan to which the company contributes. As a full time special agent for Northwestern, the taxpayer was obliged to give Northwestern first refusal on all life insurance business, provided it was

the kind Northwestern insured. Although in his particular case Northwestern did not provide office space and stenographic services as it did in the case of many other special agents, the taxpayer was allowed in lieu thereof an additional commission. He was covered by Northwestern's agents' retirement plan, the contributions for which were in part credited from his commissions. Since 1950, for purposes of the Social Security Act, as amended in 1950, the taxpayer has been treated by Northwestern as its employee, and it has paid social security taxes with respect to his services. The taxpayer's services and arrangement with Northwestern during the taxable years at issue were not different from what they were in 1950 and in subsequent years. (R. 73a-74a.)

In his income tax returns for the taxable years, the taxpayer did not include in his gross income any of the commissions received on these insurance policies, but he did deduct as necessary and ordinary business expenses the nominal expenses incident to such policies agreed to be in the amount of $5 per annum. (R. 74a.)

The Commissioner of Internal Revenue determined that the commissions received by the taxpayer on these policies should properly have been included in taxable income for the taxable years at issue, and accordingly he assessed deficiencies. (R. 74a.) The Commissioner's determination was sustained by the District Court upon the ground that it was in accordance with long-established administrative interpretation and upon the ground that this interpretation represented a correct view of the applicable law. (Pet. 10-11.)

The Court of Appeals unanimously affirmed. It concluded that the commissions received by the taxpayer upon the policies which he purchased constituted compensation for personal services and hence gross income within the meaning of Section 22(a) of the Internal Revenue Code of 1939. The circumstances of the transaction did not, in its opinion, establish a bargain purchase of insurance or "discount" as contended by the taxpayer.[2] (Pet. 14-15.) The Court of Appeals also concurred in the view of the District Court that the long-standing administrative interpretation, under which commissions received by a life insurance agent on policies which he purchased were held to constitute taxable income, was entitled to great weight. (Pet. 18-19.)

ARGUMENT

The issue presented here is simply whether commissions earned by a life insurance agent on insurance policies which he himself purchased constituted taxable income to the agent when received. The decisions below holding that such commissions did constitute taxable income are correct and are not in conflict with any decisions of this Court or of other courts of appeals.

1. Commissions earned on insurance premiums constitute income to the recipient within the broad

[2] In view of this holding, the Court of Appeals found it unnecessary to pass upon the Government's alternative contention that, even if the transaction be viewed as a bargain purchase, it was a benefit secured by virtue of an employment relationship and thus constituted taxable income.

provisions of Section 22(a) of the Internal Revenue Code of 1939. (Appendix, *infra*, p. 14). The provisions of Section 22(a), which have been held to reach "income derived from any source whatever" (*Commissioner* v. *Glenshaw Glass Co.*, 348 U. S. 426, 429-430), are certainly broad enough to include such commissions as income, and Section 29.22(a)-2 of Treasury Regulations 111 (Appendix, *infra*, p. 15) specifically provides that "commissions on insurance premiums" are income to the recipient. The taxpayer seeks to create an exception to this rule for commissions earned on policies of which he was the purchaser, but no such exception may be found either in the statutes or in the Regulations. Rather, the present controversy, when reduced to fundamentals, is the simple case of an employee receiving compensation for services rendered, one of the clearest types of taxable income.[3]

As both the Court of Appeals and the District Court found, the insurance companies for which the taxpayer acted as agent had a contractual obligation to pay the taxpayer commissions on all premiums received on policies which he procured. The companies did in fact pay the commissions earned and thus discharged their contractual obligation to the taxpayer. These commissions, both courts held, constituted payment for services rendered and thus gross income within the meaning of Section 22(a). (Pet. 10-11, 16.) The compensation which the taxpayer

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[3] As such, this case presents no constitutional question, notwithstanding the taxpayer's assertion to the contrary (Pet. 5).

was entitled to receive by way of commissions was measured solely by the business which he obtained for the insurance companies. Having procured purchasers of insurance policies, the taxpayer, as an agent, had fulfilled his part of the contract and was entitled to the commissions agreed upon.

No difference in result follows from the fact that in the present case the taxpayer was himself the purchaser of the insurance policies. He had procured or obtained business for the companies and was thus entitled to the agreed commissions on the premiums paid, regardless of the identity of the purchaser. Such commissions represented a "payment in return for services rendered" and thus constituted gross income. *Robertson* v. *United States*, 343 U. S. 711, 714. The position taken by the Government and adopted by the courts below is in accordance with an administrative interpretation which has been in existence for over forty years. In T. D. 2137, promulgated in 1915 (Appendix, *infra*, p. 15), the Commissioner ruled that commissions received by a life insurance agent on policies which he purchased represented income to the agent. In G.C.M. 10486 (1932) (Appendix, *infra*, pp. 15-17), this ruling was elaborated upon, and it was there pointed out that there is no distinction between commissions earned by an agent on policies purchased by others and the commissions earned on policies purchased by the agent himself. The ruling was reaffirmed once more in Rev. Rul. 55-273 (1955) (Appendix, *infra*, pp. 17-19) in which it was held that the same rule should apply, notwithstanding the fact that technically the in-

surance agent may be an independent contractor rather than a direct employee of an insurance company. Such long-standing administrative interpretations of the broad provisions of Section 22(a), left unchanged by repeated reenactments of the revenue laws, are entitled to great weight. *Lykes* v. *United States*, 343 U. S. 118, 126-127; *Mass. Mutual Life Ins. Co.* v. *United States*, 288 U. S. 269, 273.

The transaction under which the taxpayer received commissions on policies which he purchased cannot properly be viewed as resulting in a reduction in cost or a discount. The insurance companies in question were required by applicable law to sell policies at fixed or uniform rates without rebate either of premiums or commissions. (*Supra*, p. 3; Pet. 13, 16-17.) The companies could not, therefore, have legally agreed to sell policies to the taxpayer at a reduced cost, nor could they have agreed to rebate to him the amount of commissions which he would otherwise have earned. Instead, the companies did what the law required them to do, namely, to sell the policies at regular premium rates. The amounts which the taxpayer received were the commissions which the company was under a contractual obligation to pay, and as such, they represented taxable income to him.

It is true that the Tax Court has reached a contrary result on similar facts in *Minzer* v. *Commissioner*, 31 T. C. No. 115, and that in *Daehler* v. *Commissioner*, 31 T. C. No. 73, although involving different facts, the Tax Court has likewise apparently refused to adopt the contentions advanced by the

Commissioner.[4] The court below was cognizant of both of the cited Tax Court decisions (Pet. 17-18), the taxpayer having called attention to the *Minzer* case in its petition for rehearing, which the court below denied. On the other hand, the Tax Court, in deciding the *Minzer* case, did not have the advantage of the opinion on appeal here. The existence of these decisions by the Tax Court affords no basis for certiorari.

2. The decision of the courts below is not, as asserted by the taxpayer (Pet. 7), in conflict with the decision of the Court of Appeals for the Second Circuit in *Benjamin* v. *Hoey*, 139 F. 2d 945. That case involved a wholly distinguishable factual situation in which the taxpayer was a member of a partnership engaged in a stock brokerage business. The taxpayer there purchased some securities for his own account and paid the regular commissions thereon. All that the Court of Appeals held was that that portion of the commissions paid by the taxpayer which corresponded to his own partnership interest

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[4] We are not aware of the basis for petitioner's assertion (Pet. 7) that these cases were decided by votes of 10 to 6 and 10 to 5, respectively. The cases, as reported by the Tax Court, do not show the number of judges participating in the majority decision, nor is it the practice of the Tax Court to do so. See *Stern* v. *Commissioner*, 215 F. 2d 701 (C. A. 3d). In any event, the taxpayer appears to be in error as to the vote in the *Minzer* case, because the decision as reported indicates that seven different judges dissented from the majority decision, while the Tax Court has only sixteen judges in active service. Section 7443, Internal Revenue Code of 1954.

was in effect a payment to himself and did not result in the receipt of taxable income.

Unlike that case, however, the present situation does not involve a payment by the insurance agent to himself. The commissions earned upon the insurance policies do not, as the case of purchases of securities, represent an additional fee which the purchaser must pay. On the contrary, the purchaser of an insurance policy must pay the entire premium to the insurance company which then may or may not be legally obligated to pay a portion of the premium received to an agent for his services in procuring the purchase of such insurance. Likewise, this case, unlike the situation in *Benjamin* v. *Hoey*, *supra*, does not involve a payment by the agent to himself or to his own partnership, but rather a payment to a wholly independent third party. The portion of the premiums which the taxpayer, as an agent, later received as commissions proceeded from the contractual obligation of the insurance company to pay to him agreed compensation on insurance obtained by him from any purchaser, and it was a payment to the taxpayer by a totally different person—not by himself to himself. The taxpayer's attempt to assert a conflict between the decision below and that in *Benjamin* v. *Hoey*, *supra*, stems from a basic confusion between a payment received from a third party in return for services rendered, as here, and a payment made by a taxpayer to his own company or partnership for his own services. Obviously, in the latter situation, income may not be created by a taxpayer's payment to hir self for services; and it is

equally obvious that, as here, income does result from the performance of services for another for an agreed compensation. Properly analyzed, it is apparent that the decision below, both in principle and in result, is not in conflict with the decision of the Second Circuit in *Benjamin* v. *Hoey*, *supra*.

3. In any event, the decision below may also be sustained on the alternative ground that, if the transaction be viewed as a bargain purchase by the taxpayer, it was a bargain purchase arising out of an employment relationship and as such constituted taxable income to the extent of the reduction in premiums. Taxpayer cannot dispute, and in fact admits (Pet. 6), that the benefit which he received through what he asserts to be a reduction in cost arose solely from his status as an insurance agent. If that be true, then the reduction in cost was a benefit conferred upon the agent as an employee in recognition of services rendered. So considered, the amount of such benefit constitutes taxable income. *Commissioner* v. *LoBue*, 351 U. S. 243; *Commissioner* v. *Smith*, 324 U. S. 177; Treasury Regulations 111, Secs. 29.22(a)-1, 29.22(a)-3 (Appendix, *infra*, pp. 14-15). This result is not affected by the circumstances that for social security purposes, or under other technical standards, he may be regarded as an independent contractor rather than a direct employee. See *Commissioner* v. *Webster Corp.*, 240 F. 2d 164 (C. A. 2d). We are not here concerned with the tort liability of the insurance company, but with an employment relationship in the broad sense. The contracts under which the insurance companies desig-

nated the taxpayer as their agent to procure insurance, and agreed to pay him a stated compensation therefor, are forms of employment. The benefits derived from such employment, whether in the form of salary or in the form of a transfer of property at less than fair value, constitute compensation for services and are thus taxable income. *Commissioner* v. *LoBue, supra*; *Commissioner* v. *Smith, supra*.[5]

CONCLUSION

The petition for a writ of certiorari should therefore be denied.

Respectfully submitted,

J. LEE RANKIN,
Solicitor General.

CHARLES K. RICE,
Assistant Attorney General.

I. HENRY KUTZ,
MYRON C. BAUM,
Attorneys.

JULY, 1959.

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[5] In view of the authorities cited, the brief filed by the *amicus curiae* is in error when it states (p. 5) that benefits derived from bargain purchases by specified groups of employees do not constitute taxable income. Moreover, such bargain purchases are expressly included in gross income by the provisions of Section 29.22(a)-1 of Treasury Regulations 111.

APPENDIX

Internal Revenue Code of 1939:

SEC. 22. GROSS INCOME.

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

* * * *

(26 U. S. C. 1952 ed., Sec. 22.)

Treasury Regulations 111, promulgated under the Internal Revenue Code of 1939:

Sec. 29.22(a)-1 [As amended by T.D. 5507, 1946-1 Cum. Bull. 18]. *What Included in Gross Income.*— * * *

* * * *

If property is transferred by an employer to an employee for an amount less than its fair market value, regardless of whether the transfer is in the form of a sale or exchange, the difference between the amount paid for the property and the amount of its fair market value is in the nature of compensation and shall be included in the gross income of the employee. In computing the gain or loss from the subsequent sale

of such property its basis shall be the amount paid for the property, increased by the amount of such difference included in gross income.

* * * *

Sec. 29.22(a)-2. *Compensation for Personal Services.*—Commissions paid salesmen, compensation for services on the basis of a percentage of profits, commissions on insurance premiums * * * are income to the recipients * * *.

* * * *

Sec. 29.22(a)-3. *Compensation Paid Other Than in Cash.*—If services are paid for with something other than money, the fair market value of the thing taken in payment is the amount to be included as income. If the services were rendered at a stipulated price, in the absence of evidence to the contrary such price will be presumed to be the fair value of the compensation received. * * *

T. D. 2137, 17 Treasury Decisions 48 (1915):

Part I.—*Rulings in relation to personal income tax.*

* * * *

Commission retained by agent on his own life insurance policy.—A commission retained by a life insurance agent on his own life insurance policy is held to be income accruing to the agent, and should be included in his return of income for the assessment of the income tax.

* * * *

G.C.M. 10486, XI-1 Cum. Bull. 14 (1932):

Information is requested relative to the basis on which a ruling relating to insurance commissions was made.

The particular ruling, which is one of several rulings contained in Treasury Decision 2137, reads as follows:

> *Commission retained by agent on his own life insurance policy.*—A commission retained by a life insurance agent on his own life insurance policy is held to be income accruing to the agent, and should be included in his return of income for the assessment of the income tax.

If a life insurance company reduces the standard charge of an insurance policy to a purchaser and the relationship of employer and employee does not exist, the amount by which the policy is reduced can not be considered income at the time of purchase for the reason that it is not "gain derived from capital, from labor, or from both combined," nor "profit gained through a sale or conversion of capital assets" within the meaning of the definition of income as stated in *Eisner* v. *Macomber* (252 U. S. 189, T.D. 3010, C.B. 3, 25). The Board of Tax Appeals has held that the purchase of property at a bargain price does not result in taxable income where the sale is consummated by two persons dealing at arms' length. (See Appeal of *Manomet Cranberry Co.*, 1 B.T.A. 706, C.B. IV-1, 3.)

The reason that the commission allowed an insurance agent on a policy taken out on his own life is considered income, is that the relationship of employer and employee exists between the insurance company and the agent, and inasmuch as the insurance company is under contract to pay the agent commissions on all policies of insurance secured by him, no dis-

tinction can logically be made between a commission paid to the agent on account of a policy written on his own life and a commission paid to the agent on account of a policy written on the life of some one else. The commission is paid to the agent as compensation for services rendered as an employee, i.e., on account of business obtained, regardless of whose life is insured, and is "gain derived from labor," and therefore taxable income. Furthermore, it is immaterial whether the agent remits to the company the standard charge for such insurance (namely, the amount that would be charged any other person under like conditions) and receives a check for his commission, or whether he remits to the company the standard charge minus his commission. The net result is the same. The agent receives taxable income to the extent of the commission, either actually or constructively. It follows that the amount of commission paid by the insurance company should be reported as income by the insurance agent.

Rev. Rul. 55-273, 1955-1 Cum. Bull. 221:

Advice has been requested whether the commission retained by an insurance salesman on an insurance policy which he purchased on his life and property under the following circumstances constitutes income to him subject to withholding of Federal income taxes.

In the instant case, an insurance salesman, as an employee of a general insurance agency who is entitled to commissions on policies which he sells, purchased policies for his own protection on his life and property through the agency for which he works at the price charged by the

agency for such insurance, less the salesman's commission.

Section 22(a) of the Internal Revenue Code of 1939, provides in part as follows:

> "Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * *.

G.C.M. 10486, C.B. XI-1, 14 (1932), holds that a commission retained by an agent on his own life insurance policy is income accruing to the agent due to the fact that an employer and employee relationship existed between the agent and the insurance company and the company was under contract to pay the agent commissions on all policies secured by him.

The principles of G.C.M. 10486, *supra*, are equally applicable to the facts in the instant case. There is no real distinction merely by reason of the fact that here the salesman was an employee of an insurance agency rather than a direct employee of an insurance company.

The agency was authorized to issue insurance contracts for insurance companies, employed its own salesmen and paid them a commission on each policy they secured. An employer and employee relationship existed between the insurance agency and its salesmen and the salesmen were entitled to a commission as compensation for policies sold by them irrespective of whether such commission was received in cash or in the form of reduced costs on policies taken through the agency.

Also, there may be insurance salesmen who might be considered independent contractors. These salesmen, like other insurance salesmen, are also entitled to a commission on each policy

secured by them as compensation for their services irrespective of the manner in which received.

Accordingly, it is held that the commission retained by an insurance salesman in the form of reduced costs on an insurance policy on his life and property, which he purchased from an insurance agency or company, constitutes income to the salesman regardless of whether the salesman is an employee or independent contractor. The amount of such retained commission is subject to withholding of Federal income taxes.

U. S. GOVERNMENT PRINTING OFFICE: 1959 514160 O - 46